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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 940

CARIBBEAN EMBROIDERY COOPERATIVE, INC., SANTIAGO R. PALMER, AND MAGDALENA J. PALMER, PETITIONERS

v.

PHILIP B. FLEMING, ADMINISTRATOR OF THE WAGE AND HOUR DIVISION, UNITED STATES DEPARTMENT OF LABOR

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The District Court wrote no opinion. Its "Findings of Fact and Conclusions of Law" appear in the record (R. 30–33). The opinion of the Circuit Court of Appeals (R. 958–982) is reported in 123 F. (2d) 749.

JURISDICTION

The judgment of the Circuit Court of Appeals (R. 982) was entered on November 18, 1941. The

petition for writ of certiorari was filed on February 11, 1942. The jurisdiction of the Court is invoked under section 240 (a) of the Judicial Code, as amended.

STATUTE INVOLVED

The pertinent provisions of the Fair Labor Standards Act of 1938, c. 676, 52 Stat. 1060, 29 U. S. C., sec. 201, hereinafter referred to as the "Act," are set forth in the appendix.

QUESTIONS PRESENTED

1. Whether the trial court's decision that the petitioner, Caribbean Embroidery Cooperative, Inc., was a bona fide cooperative, controlled and owned by the worker-members who were self-employers, was properly set aside as against the weight of the evidence; this question involves also the related findings that the petitioners, Santiago and Magdalena Palmer, did not control the cooperative and were not the employers of the "worker-members."

2. Further questions urged by the petitioners, but which we think are not involved, are whether the cooperative is a "labor organization" excluded from the definition of "employer" by section 3 (d) of the Act; and whether the wage and hour provisions of the Act apply to the workers of a bona fide cooperative which they own and control as members and stockholders.

STATEMENT

On April 20, 1940, the Administrator of the Wage and Hour Division filed a complaint in the District Court of the United States for Puerto Rico pursuant to section 17 of the Act to restrain Santiago R. Palmer, Magdalena Palmer, and Caribbean Embroidery Cooperative, Inc., from violating sections 15 (a) (1), 15 (a) (2), and 15 (a) (5) of the Act (R. 2–11). Defendants were alleged to have employed plant workers and home workers in the production of goods for interstate commerce at less than the minimum wages, and to have exceeded the maximum weekly hours of employment without payment of time and one-half for overtime. The complaint also alleged that the goods so produced were shipped in interstate commerce. There were, moreover, allegations that records were not kept as required by the Act and regulations. The main issue raised by defendants' answer (R. 25–27) was that no employer-employee relationship existed between the workers and the defendants.[1] Defendants contended that the worker-members were the sole owners of the Caribbean Embroidery Cooperative, Inc., and, accordingly, self-employers, that Mr. and Mrs. Palmer were "employees or agents"

[1] The defendants also contended that the cooperative was a "labor organization" under section 3 (d) of the Act and exempt as such (R. 26). The District Court failed to pass on this contention. The Circuit Court of Appeals held that the cooperation did not come within the exception in section 3 (d) (R. 981).

of the members, and that, accordingly, neither the Cooperative nor the Palmers was an "employer" within the meaning of section 3 (d) of the Act. The underpayments and other alleged violations were admitted by stipulation (R. 27–29.)

The District Court after trial denied the injunction and dismissed the complaint[2] (R. 33–34). The court found that the defendant cooperative "was organized in good faith and is a genuine cooperative," and concluded that the individual defendants "neither jointly nor separately own nor control" the cooperative (R. 31), and that none of the defendants was an employer of the "worker-members" of the cooperative (R. 31).

The Circuit Court of Appeals reversed the District Court's judgment and directed that an injunction issue against the three petitioners (R. 981). That court held that the "member-workers" were employees of the Palmers and the "cooperative," and entitled to the benefits of the Act. The Circuit Court of Appeals upon "a close examination of the record" was "led * * * irresistibly to the conclusion" that the trial court's finding that the workers and not the Palmers controlled the business was "against the clear weight of the evidence

[2] The court, however, found that relatives of the members "worked on goods of the * * * Cooperative with [its] * * * consent" and were "employees of the said cooperative within the meaning of the Act" (R. 33). The District Court, accordingly, enjoined the continued employment of such non-members in violation of the Act's wage and hour standards (R. 34).

and must be set aside" (R. 975–976). It recognized that findings of fact are not to be upset lightly (R. 960, 975). Reliance was placed, therefore, principally upon an examination of "documentary evidence," "testimony on which there is no conflict, and for the most part only the testimony of Palmer and Soltero [one of the petitioners and petitioners' attorney], so that the element of credibility will not be seriously involved" (R. 960). The court's opinion summarizes this evidence at considerable length.[3]

Since about 1931, Santiago Palmer and his wife, Magdalena Palmer, owned and operated the Caribbean Embroidery Company in San German, Puerto Rico (R. 710). They were engaged as contractors in the manufacture of needlework products for customers in the United States. Business was solicited through J. A. Garcia, a New York agent (R. 223, 224). Raw materials belonging to the company's customers were shipped to the San German plant, where they were cut to specifications and distributed through agents to women needleworkers on the Island who sewed and embroidered the handkerchiefs and other products in their homes.

[3] The Administrator also contended in both courts below that even were the corporation a genuine cooperative controlled by the workers, it would nonetheless be an "employer" within the meaning of the Fair Labor Standards Act. The Circuit Court of Appeals found it unnecessary to pass upon this question in view of its decision that the Palmers controlled the cooperative and were, therefore, the employers (R. 981–982).

The completed work was collected by the company's distributors, returned to its plant and, after laundering, ironing, and packing, was shipped back to the mainland (R. 3, 27).

The Fair Labor Standards Act was approved by the President on June 25, 1938, to become effective October 24, 1938. During the first year, a minimum hourly wage of twenty-five (25) cents was established, which thereafter became 30 cents.[4] Twenty-five cents an hour was substantially in excess of the earnings of the Palmer's employees (R. 28, 756–757, 820, 868, 870) or, indeed, of any of the needleworkers in Puerto Rico.

About the time of the passage of the Act, Juan Soltero, an attorney and accountant in Puerto Rico, made a study of the provisions of the new law (R. 911–912), and became convinced that the Puerto Rico needlework industry could not operate at the wage rates required by the law (R. 912), but that if organized into cooperative associations the Act would be inapplicable. He discussed his plan of "cooperativism" with some employers in the industry (R. 925–927) and shortly thereafter supervised the reorganization of the needlework business of one Castillo into a cooperative (R. 925–931).

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[4] By Act of June 26, 1940, c. 432, 54 Stat. 616, sec. 6 of the Fair Labor Standards Act was amended to provide for the establishment of special minimum rates for Puerto Rico. Pursuant to this amendment the Administrator issued a wage order, effective December 2, 1940, providing for a minimum hourly wage of 12½ cents for employees engaged in the processing of handkerchiefs in the home, and 20 cents for operations in the plant.

In June of 1938, Soltero discussed with petitioner Santiago Palmer the possibilities of establishing a cooperative to continue his needlework operations outside the scope of the Act (R. 711), using Palmer's factory and equipment and employing his services as manager (R. 718, 775, 928). Palmer was interested and proceeded to interest his workers (R. 715, 775). He distributed a circular among them advising that cooperatives would be outside the Wage and Hour law (R. 263–264) and told them that they would be without work unless they formed a cooperative (R. 775).

In the circular he urged the immediate organization of the cooperative "to permit us to continue working under the conditions more or less as we are working at the present time" (R. 263). The circular further stated (R. 264):

> If fortunately Puerto Rico in the near future becomes exempt from complying with the law, or that the situation in the industry is arranged in any other way, then the cooperative will be dissolved.[5] * * *

The motives of Palmer and his wife in the formation of the cooperative are revealed by letters written by them during this period (R. 223, 311–313).

[5] This statement by Palmer should be compared with the provision in the Articles of Incorporation which required that the manager "must be a person who sincerely believes in the principles of cooperativism" (R. 101). Palmer was to be and became that manager.

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These letters definitely indicate a plan to use the device of a cooperative to continue their business operations unchanged and without complying with the labor standards established by the Act.[8]

After considerable discussion of the plan by Palmer with the workers, Soltero organized the cooperative with a committee composed largely of Palmer's department heads and higher-paid employees as incorporators (R. 731–734). Palmer guaranteed Soltero's legal fees for this work (R. 134). Soltero showed Palmer the Articles and By-laws as soon as they were drawn up (R. 738). He consulted Palmer throughout the organization period and followed closely Palmer's business organization as the pattern for the new operations (R. 740, 936).

The Articles (R. 36–63) and By-laws (R. 63–132), discussed in detail in the opinion below (R.

[8] On August 15, 1938, Palmer wrote a long letter to his agent, Garcia, in New York, explaining his plans concerning the cooperative. The letter said in part (R. 313) "I gave instructions to friend Soltero to proceed immediately to the organization of the Caribbean Embroidery Cooperative, a thing which has been agreed upon by Castillo and me to see whether, in this manner, we do not have to stop our work for even a single day." He wrote that he was seeing the employees to "hasten the establishment of the cooperative, but, naturally on the basis of dealing only and exclusively with me." Garcia was advised to let the customers know that "we are taking the necessary steps to continue our business after the minimum wage law goes into effect." Secrecy was suggested so that competitors in Puerto Rico would not "get a notion to do the same."

966–973), are lengthy and complex. They purport to incorporate a "cooperative association" under the Puerto Rican laws to promote, among other things, "the knowledge and practice" of the needlework industry "as a source of income for the benefit of the workers" (R. 36). Applicants for membership were required to affirm their belief in "cooperativist principles" (R. 66, 229); and to subscribe to one share of stock, par value $10 (R. 72).

Although ostensibly following cooperative forms, real control over the business in all its phases was, by the Articles and Bylaws, vested in the Manager, Palmer,[7] limited only by the theoretical power of the Board of Directors to review his decisions. He was given power to choose supervisors (R. 282), to evaluate the efficiency of members; to suspend and discipline them (R. 70, 282); to apportion work among them in times of scarcity (R. 122). He established the schedule of *anticipos* or advances paid to the workers (R. 126) and the Bylaws empowered him to establish the contract prices (R. 127). The Board of Directors was composed

[7] Mrs. Palmer as assistant manager exercised all the manager's powers in her husband's absence (R. 103). His brother-in-law was secretary-treasurer (R. 744, 138) and on the Board of Directors and the executive committee (R. 819). The complex method provided for amending Articles or Bylaws, described by the lower court, permitted a single dominant officer or member effectively to block any change (R. 978–979).

chiefly of former supervisory employees (R. 733) and was virtually self-perpetuating.[8] In two years of operations covered by the record every important action of the manager which called for approval by the directors was approved unanimously (R. 791, 794, 821, 858, 885).

The business of the cooperative was conducted in the same manner as when Palmer was admittedly the owner (R. 756).[9] The Company's premises and equipment were leased by Palmer to the cooperative (R. 759).[10] The manufacturing process and departmental organization were in no way altered (R. 760). Distribution and sales were through the same channels (R. 760). The personnel and their duties remained unchanged (R. 756, 757, 759, 760, 843, 881), and the workers received in the form of *anticipos* and so-called dividends,[11] earnings no greater than their meager

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[8] The opinion below analyzes the provisions of the Articles and Bylaws giving the original Directors unusual powers with respect to the choice of their successors (R. 967–968, 977–978).

[9] As Palmer testified, "the business has continued and still continues almost the same as before the cooperative was established" (R. 756).

[10] In arriving at a valuation for the plant and equipment no independent appraisers were used but a committee consisting of two of Palmer's supervisory employees and his brother-in-law accepted the valuation submitted by Palmer (R. 142, 753, 890).

[11] The *anticipos* were advances on a piece-work basis similar in amounts to the rates the workers were paid by the old company (R. 756–757, 820, 868, 870, 872, 881, 899, 900). A reserve of 2 percent of gross income was set up for "divi-

wages when employees of the Caribbean Embroidery Company [12] (R. 756–757, 820, 868, 870, 881, 889, 900).

In addition to managing all the technical aspects of the venture (R. 777), the financial interest in the business was almost entirely Palmer's. The plant and equipment were his (R. 281);[13] he advanced by interest-bearing loan the working capital (R. 281, 288);[14] his "salary" as manager was 10 percent of the *gross business* (R. 284), which gave him a personal income from the business greater than it had ever been before (R. 762–763, 784); he guaranteed the performance of the contracts of the cooperative (R. 760–761, 226–228).

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dends" to members (R. 822, 823, 825). Dividends were in reality merely wages, the payment of which was delayed. For the first 14 months of operation the "direct workers" received in *anticipos*, an average of $83.60 per worker; the 18 supervisors an average of $269.10 each, and each of the 3 office workers $811.50. In addition, the average dividend of "direct" workers was $5.33; the supervisor's share averaged $86.04; and the office worker's $259.48. These computations are made from the annual reports of the auditor (R. 496–532).

[12] "*A Report on Puerto Rico: The Needlework Industry*" prepared in the Wage and Hour Division in 1940, which was cited by petitioners in their brief below (R. 976), found from a survey made by the United States Department of Labor in 1933–1934 that 84 percent of the home workers "were earning 3 cents or less per hour."

[13] The plant and equipment were valued, for purposes of computing the rental, at $25,000 (R. 751, 753).

[14] By the loan contract Palmer agreed to lend up to $20,000 at 6 percent interest (R. 288).

By the management contract there was delegated to Palmer subject to the Board's approval "all the necessary powers" to direct the venture (R. 282). That contract could be terminated by either party on 30 days' notice (R. 285), and termination of the management contract permitted total rescission of the loan agreement (R. 283, 290).[15] In that case the debt became due, and Palmer was empowered to take over the cooperative "until the total liquidation of the debt" (R. 283).

The financial interest of the members was meager. As of December 15, 1939, paid-up capital amounted to $1,224.71 (R. 500), and organization expenses had consumed $1,031.58 (R. 502). In March 1940, about 18 months after the formation of the cooperative, only 20 members out of 1,335 owned fully paid-up ($10) shares (R. 767). In September 1940, at the time of the trial, only "100 to 150" of the some 1,200 home worker-members had paid the $2.50 required for the right to vote (R. 782).[16]

The participation by the members in the control of the cooperative was as slight as their financial interest. The workers, largely illiterate and uninformed, understood little of the elaborate arrangements (R. 863, 933, 866, 867). Only one

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[15] The lease also was apparently terminable in this event. (R. 296; cf. R. 285).

[16] At the only general assembly in February 1940, 183 out of a membership of over a thousand were entitled to vote and only 116 exercised the right (R. 494, 462–465, 481, 483).

general assembly of the workers was held—14 months after the cooperative was organized (R. 736). A small percentage of members attended, and, as has been indicated, few were qualified to vote. Each "process" or class of workers was entitled to one representative on the Board of Directors (R. 91). The home workers,[17] who numbered about a thousand (R. 494), were entitled to no larger number of representatives on the Board than the three members (R. 494) of the stamping or office department. The numerous committees, including the Executive Committee, had only advisory functions (R. 107–117). The Executive Committee could "not make decisions that would obligate the Manager * * *" (R. 109). The members of the Board of Directors, because of their economic dependence upon Palmer, were in no position to and never challenged Palmer's control (R. 821, 794, 858, 885).

All that the illiterate workers understood of the elaborately organized cooperative set up by Palmer and Soltero was that unless they were members they could not work (R. 866–867, 863). Palmer, on the other hand, "spoke as a man who had the power of life and death over the cooperative and

[17] For the first year after the Act was passed no home workers were admitted to membership since it was believed they were not the cooperative's employees (R. 765); only after the Wage and Hour Division announced its opinion that they were employees of the cooperative and not of the distributors was a drive undertaken to enlist them as members (R. 764).

could dictate terms to it," as the court below put it (R. 976).

A short summary of the facts cannot do justice to the large number of contemporary documents and the mass of other evidence in the record, which show irresistibly that after the formation of the cooperative, as before, Palmer ran the business. The workers continued to be employed by him. The form was changed but not the substance of the relationship. There was no break in the continuity of the employment or of the substandard labor practices which the Fair Labor Standards Act outlawed.

ARGUMENT

1. The petition raises no questions of general importance. The decision below turns upon the facts of this particular case. It is not disputed that if the Cooperative was a sham, set up and controlled by Palmer, the petitioners are employers subject to the provisions of the Act.[18] The primary question is whether the Circuit Court of Appeals properly concluded that this record plainly required a holding that the cooperative was not genuinely controlled by the employees. The evidence summarized in the Statement, *supra,* shows indisputably that the court below reached the correct

[18] It is, of course, the substance of the relation and not the form which controls the application of the statutory provisions. *Gregory* v. *Helvering*, 293 U. S. 465; *Utility Coal Co.* v. *Rogez*, 170 Okla. 264, 39 P. (2d) 60; *Montello Granite Co.* v. *Industrial Comm.*, 227 Wis. 170, 278 N. W. 391.

conclusion. The Circuit Court of Appeals' refusal to sanction a device designed to evade the Act by changing the form of petitioners' business while preserving all its previous attributes plainly presents no question worthy of review.

It is well settled that where the district court's findings of fact [19] are clearly erroneous, the Circuit Court of Appeals may set those findings aside. *Aetna Life Ins. Co.* v. *Kepler,* 116 F. (2d) 1, 5 (C. C. A. 8); *Beckley National Bank* v. *Boone,* 115 F. (2d) 513 (C. C. A. 4); *Kuhn* v. *Princess Lida of Thurn and Taxis,* 119 F. (2d) 704 (C. C. A. 3); *Keller* v. *Potomac Electric Co.,* 261 U. S. 428, 444. Rule 52 (a) of the Federal Rules of Procedure [20] expressly so provides.

2. Petitioner contended in both courts below that a cooperative association is a "labor organization" and is excluded from the definition of an employer under Section 3 (d) of the Act. The trial court did not pass upon this contention. The Circuit Court of Appeals concluded that since the Palmers controlled the cooperative it was not a "labor or-

[19] Although denominated "Findings of Fact," these expressions of the trial court are in reality either conclusions of law or inferences from the essentially undisputed facts. Although perhaps not required to, the Circuit Court of Appeals, nevertheless, did accord the court's findings the same respect which properly attaches to a trial court's appraisal of conflicting evidence (R. 960, 975–976, 980).

[20] See also, note of Advisory Committee to Rule 52 (a), 28 U. S. C., p. 2640.

ganization within the meaning of Section 3 (d)" (R. 981). Accordingly it was not called upon to, and did not, decide the question petitioners seek to raise as to whether a genuine labor cooperative might be a labor organization.[21] Nor did the court below find it necessary to consider respondent's contention that the Act was applicable to petitioners even if the cooperative was genuinely owned and controlled by its members. These questions would not be before this Court unless it overturned the decision below as to the exercise of control by the Palmers rather than by the employees.

CONCLUSION

The petition presents no question of general importance, and there is no conflict of decisions; it should therefore be denied.

Respectfully submitted.

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MARCH 1942.

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[21] The purpose of the exception in Section 3 (d) obviously was to avoid any question of employment relationship between a *labor union* and its members. Cf. National Labor Relations Act, Section 2 (2), 49 Stat. 450, 29 U. S. C. Section 152; S. Rep. 573, p. 6, 74th Cong., 1st Sess.